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In the Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW, PETITIONER

v.

JOHN GILBERTSON, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION AS AMICUS CURIAE

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QUESTION PRESENTED

Whether the statute of limitations for implied private actions under the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. 240.10b-5, should be drawn from state law or from an express limitations period found in the federal securities laws.

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INTEREST OF THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission is responsible for the administration and enforcement of the federal securities laws. This case presents the issue whether the statute of limitations for implied private actions under the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934 (Exchange Act or 1934 Act), 15 U.S.C. 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. 240.10b-5, should be drawn from state law, or from an express limitations period found in the federal securities laws. Private actions provide " 'a most effective weapon in the enforcement' of the securities laws and are 'a necessary supplement to Commission action.' " *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 310 (1985), quoting *J.I. Case Co.* v. *Borak*, 377 U.S. 426, 432 (1964). The Commission has a strong interest, therefore, in the development of principles governing such private actions that promote, rather than impede, the purposes of the securities laws.

STATEMENT

1. From late 1979 through mid-1981, respondents purchased units in one or more of seven similar limited partnerships. The partnerships bought, and then leased to others, computer hardware and software, and were designed to provide tax advantages for investors. Petitioner is a law firm that helped organize the partnerships and provided legal services, including preparing the tax opinion. Pet. App. 28A-30A.

The partnerships failed. In addition, respondents later learned that they did not realize tax benefits. In 1982 and 1983, respondents were notified that the Internal Revenue Service was investigating the partnerships. Pet. App. 31A-32A. In 1985, according to respondents, fraud was uncovered following the IRS's disallowance of tax benefits because of overvaluation of partnership assets and lack of profit motive. See Resp. C.A. Joint Reply Br. 12-14.

2. On November 3, 1986, respondents filed complaints in the United States District Court for the District of Oregon.[1] The complaints alleged that the offering memoranda misrepresented the tax consequences of the investments, the profitability of the partnerships' business, the marketability of the software, and the accuracy of equipment appraisals, thereby violating, *inter alia*, Section 10(b) of the Exchange Act and Rule 10b-5. Pet. App. 32A-33A.

On petitioner's motion for summary judgment, the district court held that respondents' Section 10(b) claims were barred by the applicable statute of limitations. The court applied Oregon's two-year period governing fraud claims, subject to tolling until the injured party had "actual or inquiry notice" of the facts supporting the complaint. Because the court found that respondents were on inquiry notice of fraud as early as October 1982—more than four years before filing suit—the court concluded that respondents' claims were time-barred. Pet. App. 35A-43A.

[1] On June 4, 1987, a third complaint was filed by respondent Anthony Catalan. The district court consolidated the three actions for discovery and pretrial proceedings. Resp. C.A. Joint Br. 5 n.4.

3. The court of appeals reversed, holding that there were unresolved factual issues regarding when respondents discovered or should have discovered the alleged fraud that precluded summary judgment. Pet. App. 12A-18A. The court thereby rejected petitioner's argument that a federal limitations period, drawn from the Exchange Act, of one year from discovery, but no more than three years from the violation, should apply to Rule 10b-5 claims. See Pet. C.A. Joint Br. 14-16, citing *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.), cert. denied, 488 U.S. 849 (1988). The court concluded that in the Ninth Circuit the "analogous forum state statute of limitations period continues to govern § 10(b) claims." Pet. App. 12A.

SUMMARY OF ARGUMENT

The borrowing of state limitations periods for Section 10(b) and Rule 10b-5 private actions has generated widespread, persistent confusion in the lower courts, and has made litigation under these provisions needlessly complex and unpredictable. Recently, three courts of appeals, inspired by this Court's recent formulation of the analysis for selecting statutes of limitations for federal claims having no express period, have selected a limitations period from federal law. Although we disagree with those courts' selection of the one-and-three-year periods dating from the original securities acts, we agree that a uniform federal period should govern private Section 10(b) actions, and we believe that the five-year statute of limitations contained in Section 20A of the Exchange Act, enacted in the Insider Trading and Securities Fraud Enforcement Act of 1988, best accommodates the competing interests.

A federal limitations period should be borrowed when it governs a claim that is more analogous to the right at issue than is any state claim, and when policy concerns and litigation practicalities make the federal period significantly better for securing the pertinent federal inter-

ests. Section 20A, which codifies a right of action for certain insider trading violations, satisfies those requirements. It represents the only occasion on which Congress has provided an express private right of action for violations of Section 10(b). In taking that step, Congress enacted a statute of limitations of five years from the last transaction that is the subject of the violation. Not only are the elements of a Section 10(b) violation under Section 20A the same as in other Section 10(b) claims, but the policy balance that Congress struck in Section 20A, in establishing the appropriate length of time to sue for certain insider trading violations, readily applies to the general category of violations covered by Section 10(b). Finally, borrowing Section 20A's limitations period promotes the federal interest in uniform and efficient enforcement of the securities laws throughout the Nation.

The competing federal alternative is the one-and-three-year periods provided when Congress enacted the securities laws over half a century ago. Not only do these periods represent a far more remote appraisal of limitations policies, they also apply expressly to rights of action that are not as closely analogous to Section 10(b) as the Section 20A remedy. Moreover, applying the one-and-three-year provisions at this late date would substantially shorten the prevailing limitations periods borrowed from state law and would thereby impair investor protection.

Selecting the one-and-three-year periods would also stimulate new limitations disputes in Section 10(b) litigation, as courts and litigants struggle to determine which of two limitations periods (the five year or the one-and-three year) governs a particular case. The likely proliferation of those disputes runs counter to the very reasons for selecting a uniform federal period for Section 10(b) cases in the first place. Finally, adoption of the Section 20A period is consonant with the consistent theme of the securities laws of ensuring repose at a definite and predictable time, thus guarding against lingering and stale claims.

ARGUMENT

THE STATUTE OF LIMITATIONS GOVERNING RULE 10b-5 PRIVATE ACTIONS SHOULD BE DRAWN FROM THE FIVE-YEAR PERIOD FOUND IN SECTION 20A OF THE SECURITIES EXCHANGE ACT

A. The Traditional Approach of Borrowing State Limitations Periods Under Rule 10b-5 Has Produced Confusing and Inconsistent Results

Congress did not expressly create a private cause of action under Section 10(b); accordingly, there is no express limitations period for implied actions under Rule 10b-5.[2] Until recently, courts faced with limitations questions under Rule 10b-5 routinely turned to the state limitations period governing what was thought to be the most appropriate analogy to the federal claim. This "borrowing" of state law accorded with the traditional practice of looking to the law of the forum state to provide a limitations period for federal claims when federal law is silent on the applicable limitations period. *American Pipe & Constr. Co.* v. *Utah*, 414 U.S. 538, 556 n.27 (1974); *Auto Workers* v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 703-705 (1966); *Holmberg* v. *Armbrecht*, 327 U.S. 392, 395 (1946). On two occasions, this Court noted the prevailing practice under Rule 10b-5 of applying state limitations periods; in neither case did the Court consider the appropriateness of that practice or the practical difficulties it engenders. See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 210-211 & n.29 (1976); *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 384 & n.18 (1983).

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[2] See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 196 (1976). Shortly after the Commission adopted Rule 10b-5, a district court held that there was an implied right of action under the Rule. *Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946). Since that time, an implied right of action under Rule 10b-5 has been uniformly recognized by courts and sanctioned by congressional acquiescence. *Basic Inc.* v. *Levinson*, 485 U.S. 224, 230-231 (1988). The existence of the implied right of action is today "simply beyond peradventure." *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 380-381 & n.10 (1983).

Experience has revealed, however, that the borrowing of state limitations periods for Rule 10b-5 produces confusing and inconsistent results. The resort to state limitations periods requires an assessment of which variety of state claim furnishes the most suitable "analogy" to the Rule 10b-5 claim. Courts have disagreed, however, on the analytical approach to use in searching for the proper analogue.[3] Since there is a wide variety of potentially analogous state law claims, the differing methods for discerning the limitations period have resulted in borrowing several different types of statutes, ranging in length from one to ten years.[4]

Early cases generally applied the periods governing common law fraud.[5] Two courts of appeals continue to

[3] Some courts apply a "substantive resemblance" test, which examines the similarity of the elements of the state and federal claims; other courts apply a "commonality of purpose" test, which examines the similarity of the policies vindicated by the two claims. See generally Note, *Limitation Borrowing in Federal Courts*, 77 Mich. L. Rev. 1127, 1136-1139 (1979); 5C A. Jacobs, *Litigation and Practice Under Rule 10b-5* § 235.02 (rev. 2d ed. 1990). The two approaches frequently lead to divergent results. Compare *O'Hara* v. *Kovens*, 625 F.2d 15 (4th Cir. 1980) (using "commonality of purpose" approach and selecting state blue sky law period), cert. denied, 449 U.S. 1124 (1981), with *Wood* v. *Combustion Eng'g, Inc.*, 643 F.2d 339 (5th Cir. 1981) (applying "substantive resemblance" test and selecting state fraud period).

[4] See *O'Hara* v. *Kovens*, 625 F.2d at 18 (applying the one-year Maryland blue sky law limitations period, Md. Corp. & Ass'ns Code Ann. 11-703(f)); *Denny* v. *Performance Sys., Inc.* [1971-1972] Fed. Sec. L. Rep. (CCH) 93,387 (M.D. Tenn. 1971) (applying Tennessee's ten-year limitations period governing fraud, Tenn. Code Ann. § 28-310); see generally American Bar Association, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 646 (1985). See also Gov't Amicus Br. App. 1a-4a, *Lebman* v. *Aktiebolaget Electrolux*, No. 88-1114, cert. denied, 109 S. Ct. 3214 (1989). (We have provided the parties here with a copy of our brief in *Lebman*.)

[5] The first case of which we are aware to consider the applicable statute of limitations for Section 10(b) claims was *Osborne* v. *Mallory*, 86 F. Supp. 869 (S.D.N.Y. 1949). There, the court applied New York's six-year statute of limitations governing fraud. The first appellate court to consider the issue also chose the New York

follow that approach,[6] although more recently courts have gravitated toward borrowing the limitations periods governing blue sky private remedies.[7] Other courts of appeals, however, apply either the forum state's blue sky limitations period or the state's common law fraud period depending on the State within the circuit.[8] One court of appeals applies the period governing personal injury actions.[9]

The unpredictability fostered by inconsistent approaches to selecting the applicable period is exacerbated by the uncertainty surrounding subsidiary issues. Conflict-of-laws principles, as applied to securities transactions touching many States, make matters particularly unpredictable. Further uncertainty can result when the borrowed state law has been changed or amended. Confused and inconsistent approaches to questions such as tolling inject another level of uncertainty.[10] Deciding which features of state periods to adopt "wastes untold

six-year statute of limitations. *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951).

[6] *Nesbit* v. *McNeil*, 896 F.2d 380 (9th Cir. 1990); *Bath* v. *Bushkin, Gaims, Gaines & Jonas*, 913 F.2d 817 (10th Cir. 1990).

[7] See *O'Hara* v. *Kovens*, *supra*; *Morris* v. *Stifel, Nicolaus & Co.*, 600 F.2d 139 (8th Cir. 1979); *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977); see also *Friedlander* v. *Troutman, Sanders, Lockerman & Ashmore*, 788 F.2d 1500 (11th Cir. 1986).

[8] Compare *Herm* v. *Stafford*, 663 F.2d 669 (6th Cir. 1981) (applying Kentucky's three-year limitations period governing blue sky law claims), with *Gaudin* v. *KDI Corp.*, 576 F.2d 708 (6th Cir. 1978) (applying a four-year limitations period from Ohio's general fraud statute). Compare *Wood* v. *Combustion Eng'g, Inc.*, *supra* (applying a two-year limitations period governing claims under the Texas actionable fraud statute), with *Jensen* v. *Snellings*, 841 F.2d 600 (5th Cir. 1988) (applying Louisiana's two-year blue sky law period).

[9] *Maggio* v. *Gerard Freezer & Ice Co.*, 824 F.2d 123 (1st Cir. 1987).

[10] See Special Project, *Time Bars in Specialized Federal Common Law: Federal Rights of Action and State Statutes of Limitations*, 65 Cornell L. Rev. 1011, 1084-1095 (1980).

hours." *Norris* v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), cert. denied, 484 U.S. 943 (1987).

Recently, the Second, Third, and Seventh Circuits have charted a new course.[11] Those courts have held that the limitations periods governing certain of the express causes of action under the federal securities laws are the most appropriate source from which to draw a limitations period for Rule 10b-5 actions. We disagree with those courts that some variation of the one-year-from-discovery, but no-more-than-three-years-from-the-violation periods, provided more than a half century ago in the original securities acts, is the appropriate limitations period for Rule 10b-5 claims. We do believe, however, that a uniform federal limitations period should be applied to such private actions. In our view, the five-year limitations period in Section 20A of the Exchange Act, enacted in the Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, § 5, 102 Stat. 4681, affords Congress's most recent views on the accommodation of competing interests, provides the closest federal analogy, and promises to yield the best practical and policy results in Rule 10b-5 litigation.[12]

B. The Statute Of Limitations For A Federal Claim Having No Express Limitations Period May Be Drawn From Federal Law In Appropriate Cases

In a recent series of decisions, this Court has clarified the analytical framework for determining the appropriate statute of limitations when a federal statute is silent with respect to the applicable limitations period. "[A] clear majority of the Court [has] rejected [the] single path" of resorting only to state law, *Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S.

[11] See *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.), cert. denied, 488 U.S. 849 (1988); *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990), petition for cert. pending, No. 90-526; *Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990).

[12] Section 20A of the Exchange Act, 15 U.S.C. 78t-1, is reproduced in the appendix to this brief.

143, 146 (1987), and has ruled that the Court's task is to select "the most suitable statute or other rule of timeliness from * * * [a] source" in state or federal law. *DelCostello* v. *International Bhd. of Teamsters*, 462 U.S. 151, 158 (1983).[13]

The first step of the inquiry is to determine "whether all claims arising out of the federal statute 'should be characterized in the same way, or whether they should be evaluated differently depending upon the varying factual circumstances and legal theories presented in each individual case.'" *Agency Holding Corp.*, 483 U.S. at 147; *Reed* v. *United Transp. Union*, 488 U.S. 319, 325-326 (1989) (adopting uniform characterization where necessary to avoid "[t]ime-consuming litigation as to [a] collateral question" that would divert resources and discourage the assertion of claims under Section 101(a)(2) of the Labor Management Reporting and Disclosure Act, 29 U.S.C. 411(a)(2)).[14] The characterization of a federal claim for this purpose is usually governed by fed-

[13] This inquiry is not one into actual "legislative intent"; as this Court has recognized, in the usual case where Congress has failed to supply a limitations period, there is no indication of congressional intention on the issue at all. *DelCostello*, 462 U.S. at 158-159 n.12. Moreover, when an action is implied under a regulation, as is the case with Rule 10b-5, there is even less likelihood that Congress harbored an "intention" on a subsidiary procedural detail such as a limitations period. Thus, the issue does not turn on an inquiry into what statute of limitations the 73d Congress would have selected for Section 10(b); that Congress could not, in reason, have anticipated the current scope of Rule 10b-5. See *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 721, 737 (1975) (recognizing that the intent of the 73d Congress in 1934 does not afford insight into the proper construction of Rule 10b-5); cf. *Huddleston*, 459 U.S. at 385-386 (noting more recent congressional ratification of Rule 10b-5). See also Gov't Amicus Br. 9 n.14 in *Lebman* v. *Aktiebolaget Electrolux*, No. 88-1114, cert. denied, 109 S. Ct. 3214 (1989).

[14] See also *Wilson* v. *Garcia*, 471 U.S. 261 (1985) (selecting a uniform state personal injury analogy for all claims arising under 42 U.S.C. 1983); *Owens v. Okure*, 488 U.S. 235 (1989) (clarifying that the general or residual personal injury statute, rather than the intentional torts statute, should apply in actions under Section 1983).

eral law. *Agency Holding Corp.*, 483 U.S. at 147; *Wilson* v. *Garcia*, 471 U.S. 261, 269-270 (1985).

The second step is "whether a federal or state statute of limitations should be used." *Agency Holding Corp.*, 483 U.S. at 147. In view of the Court's historical borrowing of state law, it can generally be assumed "that Congress intends by its silence that we borrow state law." *Ibid.* However, " 'state statutes of limitations can be unsatisfactory vehicles for the enforcement of federal law,' " *ibid.*, quoting *DelCostello*, 462 U.S. at 161, in which event a federal statute may supply the better choice.

> [R]esort to state law remains the norm for borrowing of limitations periods. Nevertheless, when a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes, and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking, we have not hesitated to turn from state law.

DelCostello, 462 U.S. at 171-172.

Four Terms ago, the Court applied that two-step analysis and held that the Clayton Act limitations period, 15 U.S.C. 15b, rather than state statutes of limitations, should govern civil RICO claims. *Agency Holding Corp.*, 483 U.S. at 148-157. See also *DelCostello*, *supra* (applying limitations period provided in Section 10(b) of the National Labor Relations Act to Section 301/fair representation claims); *Occidental Life Ins. Co.* v. *EEOC*, 432 U.S. 355 (1977) (refusing to apply a state statute of limitations to EEOC enforcement actions); *McAllister* v. *Magnolia Petroleum Co.*, 357 U.S. 221 (1958) (applying federal limitations period to unseaworthiness action under maritime law); *Holmberg* v. *Armbrecht*, *supra* (applying federal doctrine of laches, rather than state limitations period, to equitable enforcement of federal right). Here, the same principles mandate the adoption for Section 10(b) and Rule 10b-5 of the five-year limitations period found in Section 20A of the Exchange Act.

C. The Five-Year Statute of Limitations Drawn From Section 20A Should Govern All Rule 10b-5 Claims

1. *All private Rule 10b-5 claims should be characterized in a consistent way.* Applying the first step in the analysis, we believe that all Rule 10b-5 claims deserve a consistent characterization for selecting the appropriate statute of limitations. Like RICO and Section 1983, Section 10(b) and Rule 10b-5 "encompass numerous and diverse topics and subtopics." *Data Access*, 843 F.2d at 1543. An action under Section 10(b) and Rule 10b-5 "can be brought by a purchaser or seller of '*any* security' against '*any* person' who has used '*any* manipulative or deceptive device or contrivance'." *Huddleston*, 459 U.S. at 382. This sweeping language encompasses claims that, on their particular facts, may be analogized to actions for common law fraud, breach of fiduciary duty, breach of contract, misappropriation, and violations of blue sky laws, among others. See p. 24 n.36, *infra* (describing examples of Rule 10b-5 claims).

In view of the broad remedial purposes animating the federal securities laws, see, *e.g.*, *Huddleston*, 459 U.S. at 386-87, legal rules that serve the goal of "facilitating Rule 10b-5 litigation" promote the "congressional policy embodied in the 1934 Act." *Basic Inc.* v. *Levinson*, 485 U.S. at 245. Protracted disputes over the collateral issue of the appropriate statute of limitations disserve the legislative purpose of facilitating an effective remedy for defrauded investors. Under these circumstances, uniform characterization "is required to avoid intolerable 'uncertainty and time-consuming litigation.' " *Agency Holding*, 483 U.S. at 150, quoting *Wilson* v. *Garcia*, 471 U.S. at 272.

2. *No state law claim provides a suitable analogy for Rule 10b-5 claims.* For many of the same reasons, there is no adequate state law analogy for Rule 10b-5 claims. The inability of the lower courts to agree on an appropriate period, despite decades of litigation, highlights the shortcomings of state law. A comparison of the two leading contenders—common law fraud and blue sky law—serves to illustrate the problem.

Common law fraud actions initially appealed to courts seeking a Rule 10b-5 analogue. Yet, this Court has observed that common law fraud doctrines were developed in contexts "light years away from the world of commercial transactions to which Rule 10b-5 is applicable." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 744-745 (1975). Indeed, one of Congress's paramount objectives in enacting Section 10(b) was to "rectify perceived deficiencies in the available common law protections by establishing higher standards of conduct." *Huddleston*, 459 U.S. at 389. Thus, "[a]ctions under Rule 10-b are distinct from common-law deceit and misrepresentation claims * * * and are in part designed to add to the protections provided investors by the common law." *Basic Inc.* v. *Levinson*, 485 U.S. at 244 n.22. In view of these differences, common law fraud provides only a rough analogy to claims under Section 10(b) and Rule 10b-5—and the limitations period governing common law fraud provides only a crude approximation of the balance of competing interests at stake in Section 10(b) private litigation.

Likewise, the blue sky civil remedy provisions generally vary in significant respects from claims under Section 10(b) and Rule 10b-5. Many jurisdictions have adopted antifraud provisions patterned after Section 410(a) of the Uniform Securities Act, which provides an express private right of action similar to Section 12(2) of the Securities Act of 1933 (Securities Act or 1933 Act), 15 U.S.C. 77*l*(2). Like Section 12(2), but unlike Section 10(b), these blue sky provisions do not require proof of scienter, reliance, or causation. Significantly, blue sky civil remedy provisions "come[] in a variety of shapes and sizes" varying considerably from state to state. L. Loss, *Fundamentals of Securities Regulation* 877-879 (2d ed. 1988). In view of the nuances and variation among the state securities laws, their limitations periods do not provide a promising source for a uniform, predictable rule.

3. *Section 20A of the Exchange Act provides a closer analogy to Rule 10b-5 than do state law alternatives.*

Here, as in *Agency Holding Corp.*, 483 U.S. at 150, "it is a *federal* statute that offers the closest analogy" to Rule 10b-5—Section 20A of the Exchange Act, 15 U.S.C. 78t-1. Indeed, Section 20A is more than a mere "analogy." It provides an express cause of action (on behalf of certain victims of insider trading) based on violations of the very provisions at issue here, Section 10(b) and Rule 10b-5. Section 20A codifies an express private right of action on behalf of persons trading contemporaneously in the market against "[a]ny person who violates any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information."[15] Section 20A(b)(4), 15 U.S.C. 78t-1(b)(4), sets forth an express statute of limitations:

> No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

Unlike any other express action in the federal securities laws, Section 20A specifically authorizes recovery for a particular type of Rule 10-5 violation. Actions brought under Section 20A, based on Rule 10b-5 violations, therefore require the plaintiff to establish the same elements of the violation as any claim brought under Rule 10b-5: (1) that the defendant engaged in fraud or manipulation, *Santa Fe Indus., Inc.* v. *Green*, 430 U.S. 462, 471-474 (1977); (2) that he acted with scienter, *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 193 (1976); (3) that the misconduct related to a "material" fact, *Basic Inc.* v. *Levinson*, 485 U.S. at 238; and (4) that the misconduct occurred "in connection with" a securities transaction, *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. at

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[15] A principal purpose of this provision was "to overturn court cases which [had] precluded recovery for plaintiffs where the defendant's violation is premised upon the misappropriation theory [of insider trading]." H.R. Rep. No. 910, 100th Cong., 2d Sess. 26 (1988), citing *Moss* v. *Morgan Stanley*, 719 F.2d 5 (2d Cir. 1983), cert. denied, 465 U.S. 1025 (1984).

749.[16] Moreover, a claim under Section 20A, when premised on a violation of Rule 10b-5, is designed to further the same federal antifraud policies vindicated in any lawsuit under Section 10(b).[17]

Although Section 20A is addressed solely to insider trading, that consideration does not undermine its comparability to other Rule 10b-5 violations for purposes of choosing a limitations period. Contrary to the Second Circuit's view that Section 20A has "no relationship" to many types of Section 10(b) claims, *Ceres Partners* v. *GEL Associates*, No. 89-7666 (Nov. 8, 1990), slip op. 7271, the correspondence of elements required to establish a *violation* creates a compelling "analogy" between Section 20A and Rule 10b-5 generally; no other express cause of action under the securities laws reflects that match.[18] Moreover, the competing policies that Congress had to balance in enacting Section 20A's five-year limitations period, in the context of legislation dealing with insider trading, carry over to other forms of action based on Rule 10b-5. As the Second Circuit noted, a central

[16] Section 20A also imposes certain additional requirements (such as that the defendant and plaintiff have purchased or sold the same class of securities contemporaneously), but those differences from the requirements of other Rule 10b-5 actions are relatively minor.

[17] Congress enacted Section 20A knowing that insider trading violations involving Rule 10b-5 form a particular category of the general right of action under Rule 10b-5. See H.R. Rep. No. 910, 100th Cong., 2d Sess. 8 (1988).

[18] Nor does Congress's choice of a five-year period for Section 20A imply that other types of Rule 10b-5 claims should be subject to a different limitations period. In the statute itself, Congress signaled its intent that courts should continue to develop the incidents of the law governing the implied rights of action such as that recognized under Rule 10b-5. See 15 U.S.C. 78t-1(d). The legislative history, in discussing the substantive law, explained that Congress intended to "avoid * * * freezing the law or in any way restricting the potential rights of action which have been implied by the courts in this area," but instead to give "the courts leeway to develop such private rights of action in an expansive fashion in the future." H.R. Rep. No. 910, *supra*, at 27. See also 134 Cong. Rec. H7470 (daily ed. Sept. 13, 1988) (remarks of Rep. Lent); *id.* at S17,220 (daily ed. Oct. 21, 1988) (remarks of Sen. Garn).

concern of Congress was to address "the difficulties of ferreting out evidence sufficient to prosecute insider trading cases," *Ceres Partners*, slip op. 7271. Other Rule 10b-5 plaintiffs face equally daunting problems in ferreting out evidence of fraud.[19] Consequently, Congress's accommodation of policies, in determining to limit fraud claims under Section 20A by a five-year statute, fairly reflects the appropriate balance in other Rule 10b-5 contexts as well.[20]

4. *Policy and practical considerations favor Section 20A over state law.* There are compelling reasons to reject the application of state law to Rule 10b-5 claims. A principal purpose of the Exchange Act is to regulate the securities markets, which are inherently national in scope. See *Blue Chip Stamps*, 421 U.S. at 744-745. The securities laws are built around a jurisdictional nexus to interstate commerce or the mails, and were enacted in part because no single State's laws are capable of regulating the Nation's capital markets. See 15 U.S.C. 78b. Cf. *Agency Holding Corp.*, 483 U.S.C. at 153-154. "Congress enacted a national rule against fraud because it believed that national law ought to govern multistate transactions. Returning to state law to fetch a period of limitations is inconsistent in spirit with this decision." *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1388

[19] For example, frauds based on "Ponzi" schemes can easily be concealed for several years—enough to ensure the running of a short statute of limitations for many claims. And "[a] similar situation often occurs in connection with defaulted municipal bond issues, an area of Rule 10b-5 securities fraud that may well involve more damages to investors on a national level than any other." Guin & Donaldson, *The Insider Trading and Securities Fraud Enforcement Act: Has Congress Supplied A Limitations Period Appropriate For Use In Private 10b-5 Actions?*, 47 Wash. & Lee L. Rev. 541, 569 (1990).

[20] Congress chose the same five-year limitations period for Commission penalty actions for insider trading violations. See 15 U.S.C. 78u-1(2) (authorizing penalty of up to three times profit gained or loss avoided), 78u-1(d)(5) (barring action "more than 5 years after the date of purchase or sale"). See H.R. Rep. No. 355, 98th Cong., 2d Sess. 12 (1984).

(7th Cir. 1990), petition for cert. pending, No. 90-526; see *Ceres Partners*, slip op. 7266.

Moreover, reference to state limitations periods under Rule 10b-5 results "in wholly unjustified disparities in the rights of parties litigating identical claims in different states." American Bar Association, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 647 (1986) (hereinafter *ABA Report*). Multidistrict cases and class actions starkly illuminate those disparities.[21] Not only are different limitations periods unfair, they also invite use of the broad venue provisions of the securities laws to engage in forum shopping. *Ibid.* Although conflicts principles and borrowing statutes may discourage abuses, the application of choice-of-law doctrines complicates an already baffling and unpredictable process. Given the multistate nature of claims under Section 10(b) and Rule 10b-5, the borrowing of state law has resulted in "complex and expensive litigation over what should be a straightforward matter." *Agency Holding Corp.*, 483 U.S. at 154.

Courts[22] and commentators[23] agree that federal policy

[21] See, *e.g.*, *In re Clinton Oil Co. Securities Litigation*, [1977-1978] Fed. Sec. L. Rep. (CCH) ¶ 96,015 (D. Kan. 1977) (transferee court in multidistrict litigation was forced to select different limitations periods for each of several consolidated actions involving the identical violation). See also *Pinney* v. *Edward D. Jones & Co.*, 735 F. Supp. 915 (W.D. Ark. 1990) (discussing five options available to courts attempting to set limitations periods applicable to non-resident class claims); *Kronfeld* v. *Advest, Inc.*, 675 F. Supp. 1449, 1457-1458 & n.21 (S.D.N.Y. 1987) (borrowing statute resulted in application of at least 26 separate statutes of limitations).

[22] See *Data Access*, 843 F.2d at 1549 ("A broker in New York, an issuer in Delaware, a purchaser in San Francisco, an accountant in New Jersey, and a lawyer in Pennsylvania should be subject to the same statute of limitations for actions based on Section 10(b) or Rule 10b-5."); *Short*, 908 F.2d at 1389 ("From the perspective of practitioners litigating cases originating in many states * * *, the situation is a nightmare."); *Norris*, 818 F.2d at 1332 (describing approaches to subsidiary limitations issues created by reference to state law as a "tottering parapet of a ramshackle edifice").

[23] *ABA Report*, *supra*, at 656; L. Loss, *supra*, at 994-996; Ruder & Cross, *Limitations on Civil Liability Under Rule 10b-5*, 1972 Duke

and the efficiency of litigation are impaired by the borrowing of state law. The use of a limitations period drawn from Section 20A eliminates the quagmire that has resulted from looking to a "grab-bag," L. Loss, *supra*, at 995, of more or less analogous state statutes. It ensures that federal interests are protected by a defined, nationally uniform limitations period that is suited to the policies underlying the securities laws.

D. The One-And-Three-Year Limitations Periods Governing Certain Express Causes of Action In The Federal Securities Laws Should Not Be Applied To Rule 10b-5

The competing federal alternative to Section 20A is some form of the one-and-three-year limitations periods applicable to the express causes of action in the 1933 Act and to certain of the express actions in the 1934 Act. Congress, acting for the first time in 1988 to codify a private right based on a Section 10(b) violation, did not select those periods. Likewise, in our view, this Court should not apply those periods to Section 10(b) private actions generally.[24]

1. *The one-and-three-year periods apply to rights of action that are not more analogous to Rule 10b-5 than is Section 20A.*

a. Rule 10b-5 differs from the express rights of action that are subject to the one-and-three-year periods in the

L.J. 1125, 1142-1150; 2 T. Hazen, *The Law of Securities Regulation* § 13.8, at 127-128, 133 (2d ed. 1990); Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 Wayne L. Rev. 635 (1967); Block & Barton, *Statute of Limitations in Private Actions Under Section 10(b)—A Proposal for Achieving Uniformity*, 7 Sec. Reg. L.J. 374 (1980).

[24] *Data Access*, which initiated the move to a federal period, was decided before Congress enacted Section 20A. Both the Second Circuit in *Ceres* and the Seventh Circuit in *Short* chose a one-and-three-year format over Section 20A. But the Seventh Circuit acknowledged that "[c]hoosing between these statutes is difficult," *Short*, 908 F.2d at 1390, and one of the primary reasons supporting that court's decision—the desire to avoid creating a conflict with the Third Circuit (*id.* at 1390-1391)—does not apply to this Court, and indeed was not even accomplished by the Seventh Circuit's holding, see pp. 22-23, *infra*.

1933 and 1934 Acts in ways that substantially undercut the force of any analogy between those rights and Rule 10b-5.[25] Sections 11 and 12 of the 1933 Act, 15 U.S.C. 77k, 77*l*, unlike Section 10(b), provide remedies that do not require the plaintiff to prove scienter, reliance, or causation and that shift certain burdens of proof to the defendant. See L. Loss, *supra*, at 883-886, 887-895, 896-900.[26] Section 9 of the 1934 Act, 15 U.S.C. 78i—unlike

[25] The 1933 Act contains one-and-three-year statutes of limitations for the express rights of action brought under Sections 11 and 12 of the 1933 Act, 15 U.S.C. 77k, 77*l*. Section 11 creates a private right of action for false registration statements. Section 12(1) creates a private right of action predicated on the unlawful sale of unregistered securities. Section 12(2) creates a private right of action for the sale of securities through false or misleading statements. Section 13, 15 U.S.C. 77m, sets forth the applicable limitations periods.

The 1934 Act contains one-and-three-year statutes of limitations for the express rights of action created under Sections 9, 18, and 29. Section 9(e), 15 U.S.C. 78i, creates a private right of action for certain proscribed types of manipulation of security prices on national securities exchanges. Section 18(a), 15 U.S.C. 78r(a), creates a private right of action for misleading statements in applications, reports, or documents filed with the Commission. Section 29(b), 15 U.S.C. 78cc(b) (added by the Act of June 25, 1938, ch. 677, § 3, 52 Stat. 1076), permits rescission of certain purchases or sales of a security in violation of the Exchange Act or rules thereunder, and provides a one-and-three-year limitations period for private rescission actions based on violations of any regulation under 15 U.S.C. 78*o*(c)(1).

[26] As this Court has recognized, Section 11 is "limited in scope", "places a relatively minimal burden on a plaintiff," and "address[es] different types of wrongdoing" than Section 10(b). *Huddleston*, 459 U.S. at 382; see *ibid.* ("a § 10(b) plaintiff carries a heavier burden than a § 11 plaintiff"). Section 12(1) is virtually a strict liability provision for violation of the registration provision of the 1933 Act, 15 U.S.C. 77e. And, for the reasons noted in the text, the Seventh Circuit's observation in *Short* that Section 12(2) "describes the offense to which Rule 10b-5 is applied," 908 F.2d at 1390, is inaccurate. In fact, the Rule 10b-5 analogue in the 1933 Act is Section 17(a), 15 U.S.C. 77q(a), for which Congress provided no express private right of action.

the flexible Section 10(b)—is aimed at a static range of particular manipulative practices, and applies *only* to securities registered on a national securities exchange (and therefore has no application to the securities offered here).[27] Section 18 of the 1934 Act, 15 U.S.C. 78r, pertains only to false or misleading reports filed with the Commission (again, irrelevant here), and, unlike Section 10(b), does not require that the plaintiff prove scienter; in fact, it shifts the burden to the defendant to show good faith.[28] In contrast, private actions under Section 10(b) ordinarily require that the plaintiff prove scienter, reliance, and causation. Indeed, the 73d Congress enacted the relatively short limitations periods for the express rights in part because of the comparatively light burden placed on a plaintiff in an action under many of the express remedy provisions.[29]

[27] Although Section 9, like Section 10(b), requires proof of scienter and causation, Section 9, as this Court has recognized, focuses narrowly "upon the amount actually paid by an investor for stock that had been the subject of manipulative activity." *Piper* v. *Chris-Craft Indus., Inc.*, 430 U.S. 1, 46 (1977); see H.R. Rep. No. 1383, 73d Cong., 2d Sess. 11 (1934). Moreover, a shorter statute of limitations for that provision may be explained by its application exclusively to securities registered on a national securities exchange, which generally have wide distribution and are closely watched by the exchanges, investors, and the media. The owner of such securities may not need an extended period of time to discover the manipulation. In any event, as commentators have recognized, the private right under Section 9(e) "has been a dead letter so far as producing recoveries is concerned." L. Loss, *supra*, at 920.

[28] Section 18 has the "narrow and particularized objective of encouraging use of and reliance upon records" filed with the Commission, *Ross* v. *A.H. Robins Co.*, 607 F.2d 545, 556 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980), and therefore extends liability only to persons who make a misstatement in a report or other document filed with the Commission.

[29] As Senator Austin explained in the course of debate:

> I inquire of the Senator * * * whether he does not recognize another exceptional circumstance in that the burden of proof is shifted around on the question of knowledge or willfulness in a misrepresentation. The committee have put the burden on the defendant, so that in this case the plaintiff does not have to

This Court has shaped the private right of action under Section 10(b) with the understanding that the one-and-three-year limitations periods do not apply to it. In *Ernst & Ernst* v. *Hochfelder*, the Court held that scienter, rather than negligence, must be established in a Section 10(b) action. As one factor supporting that conclusion, the Court noted that while the express causes of action under the 1933 Act permit recovery on a negligence theory, they are subject to "significant procedural restrictions not applicable under § 10(b)," 425 U.S. at 208-209, including the one-and-three-year limitations period. *Id.* at 210. Section 10(b) claims, the Court observed, enjoyed the benefit of state statutes of limitations that "usually are longer than the period provided under [the 1933 Act]." *Id.* at 210 n.29. Because Section 10(b) claims lack the "procedural limitations" applicable to the express causes of action, the negligence standard of those provisions could not be extended to Section 10(b) "consistently with the intent of Congress." 425 U.S. at 210. Building on the same principle, *Herman & McLean* v. *Huddle-*

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spend any time going out and seeking his evidence. All he has to prove is the fact of misrepresentation.

78 Cong. Rec. 8201 (1934). Other statements made in the debate focus on the possibility that "technical" defects in a registration statement might create liability far into the future—a concern that is inapplicable to Rule 10b-5, which requires proof of intentional fraud and applies to much more than the initial offering of securities. See *id.* at 8199 (remarks of Sen. Kean) (expressing concern that persons might wait before suing over a "technical mistake in a [registration] statement"); *id.* at 8200 (remarks of Sen. Byrnes) (expressing concern that distant suits based on a misstatement in a registration statement might deter persons from serving on boards of directors). Some Senators focused on the desirability of requiring actions to be brought within a defined period after discovery of a violation. See *id.* at 8198 (remarks of Sen. Fletcher) ("[T]he thought was that a man ought not to delay suit more than 1 year after he discovers the fraud."). It is noteworthy that this one-year period, established in 1934 before Congress had gained experience with the operation of the securities laws, has not proved persuasive in the contemporary financial environment, as is evidenced by Congress's adoption in 1988 of a straightforward five-year provision in Section 20A.

ston concluded that the rights of action under Section 10(b) and Section 11 of the 1933 Act are cumulatively available to a defrauded investor. 459 U.S. at 381-387. In reaching that conclusion, the Court again relied on the differences between Section 11 and Section 10(b)—including the fact that while Section 10(b) requires scienter, it lacks procedural restrictions, such as a short statute of limitations. 459 U.S. at 384 n.18 (state limitations period for "§ 10(b) * * * is usually longer than the period provided for § 11 actions").

b. Quite apart from the fact that engrafting the one-and-three-year periods onto Section 10(b) is inconsistent with those aspects of *Hochfelder* and *Huddleston*, it is also crucial to note that there is no single "one-and-three-year" period in the securities laws; rather, there are only multiple variations on a theme, each uniquely fashioned for a particular express right of action. See L. Loss, *supra*, at 988-991.

Section 9(e) of the 1934 Act provides a period of one year after "discovery of the facts constituting the violation," but no more than three years after "such violation." 15 U.S.C. 78i(e). Section 18(c), in contrast, starts the one-year period after discovery of facts constituting "the cause of action," and bars suits three years after the cause of action "accrued." 15 U.S.C. 78r(c). And, Section 29(b)'s one-and-three-year periods are tied to the date of the "sale or purchase" involving the violation. 15 U.S.C. 78cc(b). These variations in language can produce strikingly different results when applied to the same set of facts.[30] Section 13 of the 1933 Act, in

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[30] The date of a Rule 10b-5 "violation" need not coincide with the "accrual" of a cause of action. In *Basic Inc.* v. *Levinson*, for example, the Rule 10b-5 violation was a company's issuance of false or misleading public statements denying it was engaged in merger talks. A class action was brought on behalf of shareholders who sold their stock in the company between October 1977 (the time of the first false statement) and December 1978 (when a merger was announced). 485 U.S. at 227-228. The "violation" occurred when false statements were made; the cause of action could not have "accrued" until each shareholder actually sold his stock. The results

turn, provides still other variations for each of its express rights of action. 15 U.S.C. 77m. In particular, claims under Sections 11 and 12(2)—unlike claims under Sections 9, 18, and 29 of the 1934 Act—must be filed within one year of actual or *constructive* discovery ("after such discovery should have been made by the exercise of reasonable diligence").[31] The three-year outside periods also begin to run from different events—after the security was "bona fide offered" for Section 11, but after the "sale" for Section 12(2).[32]

Although these variations can make a critical difference for the timeliness of any particular action, the courts of appeals that have embraced the one-and-three-year periods appear not to have appreciated the quandary. The Third Circuit, leading the way in *Data Access*, purported to apply the general one-and-three-year "schema" in the Exchange Act, 843 F.2d at 1546, but ultimately adopted a limitations period of "one year after the plaintiff discovers the facts constituting the violation, and in no event more than three years after such violation", *id.* at 1550, a formulation that corresponds to Section 9(e) of the 1934 Act.[33] The Seventh Circuit,

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of applying the limitations periods of Sections 9(e) and 18(c) would therefore diverge. In contrast, Section 20A(b)(4)'s test ("date of the last transaction that is the subject of the violation") would provide far greater certainty and ease of application.

[31] A Section 12(1) claim must be brought within one year "after the violation upon which it is based," but no more than three years "after the security was bona fide offered to the public".

[32] The 1933 Act limitations periods were originally two years and ten years, Act of May 27, 1933, ch. 38, § 13, 48 Stat. 84, but Congress shortened those periods when it amended the Securities Act in 1934. 48 Stat. 908. See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 210.

[33] The court did not explain why it chose the Section 9 formulation. If the theory behind borrowing the one-and-three-year periods is that Section 10(b) and Rule 10b-5 are analogous to the *cumulative* scope of Sections 9, 18, and 29 of the 1934 Act, and Sections 11 and 12 of the 1933 Act, it is inconsistent with that rationale to conclude that the Section 9 limitations period in particular should be applied to *all* Section 10(b) claims.

following on the heels of *Data Access*, mistakenly thought that the Third Circuit had selected Section 13 of the 1933 Act; it then concluded that Section 12(2) formed the appropriate model for Rule 10b-5, and ultimately adopted Section 12(2)'s one-and-three-year limitations provision. *Short*, 908 F.2d at 1390-1391. But that provision includes a *constructive* discovery limitation on the one-year period, in conflict with the choice made by *Data Access*.[34] Finally, the Second Circuit held that Rule 10b-5 claims would be governed by "the statute of limitations provided in the 1934 Act for express rights of action under §§ 9(e) and 18(a) of that Act," *Ceres Partners*, slip op. 7274, even though the language of those two provisions differs. The three-way conflict generated by the courts of appeals underscores the futility of searching for an apt analogy in any of the express rights of action enacted in 1933 and 1934 for purposes of selecting the appropriate statute of limitations for Rule 10b-5.

2. *Policy considerations militate against the one-and-three-year system.* Applying the relatively short one-and-three-year periods frustrates important policy goals as well.[35] As the law has developed, Rule 10b-5 is vastly more important in combatting fraud than are the express remedies provided in the 1933 and 1934 Acts. Borrowing the shorter limitations periods found in those Acts for Rule 10b-5 would impede enforcement of the Rule's requirements, and would thereby impair the securities laws' function of protecting investors.

Section 10(b) and Rule 10b-5 have come to embrace a diversity of claims which could not have been envisioned in 1934. This Court has consistently construed those provisions broadly, noting that they "are obviously

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[34] In the Third Circuit, the one-year period is not subject to a constructive discovery limitation. See *Gruber* v. *Price Waterhouse*, 911 F.2d 960, 964 n.4 (1990).

[35] The Court has noted that policy considerations are relevant in delineating the contours of Rule 10b-5. See *Blue Chip Stamps*, 421 U.S. at 737, 749.

meant to be inclusive." *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 151 (1972). See *Huddleston*, 459 U.S. at 386; *United States* v. *Naftalin*, 441 U.S. 768, 773 (1979).[36] By contrast, the express remedies governed by the one-and-three-year limitations periods are much more limited in scope. Indeed, the implication of a right of action under Rule 10b-5 is justified in part because the specific liabilities created by the express causes of action in the Exchange Act "do not cover all the variegated activities with which that act is concerned." 3 L. Loss, *Securities Regulation* 1785 (2d ed. 1961).

The one-and-three-year periods, if applied to Rule 10b-5, would deprive many defrauded investors of a satisfactory opportunity to vindicate their rights. Especially in complex cases, plaintiffs often "do not discover the fraud until long after its perpetration." *ABA Report*, *supra*, at 656.[37] Violations involving financial fraud, for instance, often go undetected until the enterprise fails, an event that may occur years after the violation. Moreover, as the securities markets have grown in size and complexity, frauds have become increasingly difficult to discover.[38] Thus, we do not agree with the

[36] Section 10(b) actions can be brought against the issuer of securities for false or misleading material public statements, see *Basic Inc.* v. *Levinson*, *supra*; against accountants, lawyers, or others involved in an offering of securities, see *Huddleston*, 459 U.S. at 378; against broker-dealers by customers fraudulently induced to purchase securities, see *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 301-303 (1985); against persons who trade in the securities market while in possession of non-public information in breach of a duty, cf. *Dirks* v. *SEC*, 463 U.S. 646, 653-654 (1983); against persons who manipulate the market for securities, cf. *Santa Fe Indus., Inc.* v. *Green*, 430 U.S. 462, 476-477 (1977); and in many other situations.

[37] Indeed, even the SEC with all its investigative resources and statutory powers, including compulsory investigative processes, does not complete its investigations, on average, in less than 2.25 years.

[38] Congress recognized these developments in recent amendments to the securities laws that provide the Commission additional enforcement remedies. See The Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat.

Seventh Circuit's sanguine view that "[p]rudent investors can almost always sniff out fraud (or enough smoke to justify litigation) within three years," *Short*, 908 F.2d at 1392; in the Commission's experience, a considerable number of frauds are simply not detected within that period of time.

Because "the interests of plaintiffs in [Rule 10b-5] suits are significant," *Huddleston*, 459 U.S. at 390, and private actions "constitute[] an essential tool for enforcement of the 1934 Act's requirements", *Basic Inc.*, 485 U.S. at 231, the adequacy of a limitations period to serve the purposes of the Rule is an important consideration. In this case, application of the short one-and-three-year periods threatens to undermine the effectiveness of the Rule 10b-5 remedy. Cf. *Agency Holding Corp.*, 483 U.S. at 154 (rejecting use of "unduly short state statutes of limitations that would thwart the legislative purpose of creating an effective remedy"); *DelCostello*, 462 U.S. at 166, 167-168 (rejecting state limitations periods that were too short to vindicate federal rights).

3. *Applying the one-and-three-year periods would perpetuate uncertainty over limitations issues.* Adoption of a one-and-three-year provision would mean that actions based on Rule 10b-5 violations would be subject to two different statutes of limitations—those periods and Section 20A(b)(4). This would inevitably engender confusion. As the Seventh Circuit noted, "[c]lever lawyers could describe even a garden variety fraud as 'purchasing or selling a security while in possession of material, nonpublic information'—that is, the truth—blurring the line between the offenses and making the choice of a period of limitations difficult." *Short*, 908 F.2d at 1391.[39] Appli-

931; S. Rep. No. 337, 101st Cong., 2d Sess. 6 (1990) ("As the markets * * * have grown dramatically in size and complexity, particularly in the last decade, the SEC's law enforcement task has become increasingly difficult. Investigations involve more complex issues of fact and law."); 136 Cong. Rec. S10,011 (daily ed. July 18, 1990) (remarks of Sen. Dodd).

[39] The Seventh Circuit erroneously downplayed that confusion, however, because it incorrectly assumed (908 F.2d at 1391) that

cation of different periods to different types of claims based on Section 10(b) will give parties an incentive to engage in "artful pleading" in the hope of "persuad[ing] the court that the facts and legal theories of a particular * * * claim" fall within Section 20A's longer limitations period. *Owens* v. *Okure*, 488 U.S. 235, 240 (1989). Courts and parties would be called upon to wrestle with these characterization questions—a result which runs counter to the reasons for choosing a uniform federal rule in the first place. Section 20A eliminates those problems.

The problem with selecting the one-and-three-year periods is accentuated in Rule 10b-5 insider trading cases. In Section 20A, Congress codified a Rule 10b-5 cause of action for contemporaneous traders; the legislative history, however, acknowledged that "there clearly are injuries caused by insider trading to others beyond contemporaneous traders." H.R. Rep. No. 910, *supra*, at 27. For example, the Committee Report cited *Anheuser-Busch Co.* v. *Thayer*, No. CA3-0794-R (N.D. Tex. 1986), in

only an individual "insider," not the issuer itself, can be liable under Section 20A (in fact, both can be liable), and because it noted that persons suing under Section 20A "must accept the limitations of that statute, including the restriction of damages to the defendants' profit (as opposed to the plaintiff's loss)." *Ibid.* To a plaintiff who misses the three-year deadline, however, it is Section 20A or nothing; hence, the availability of damages, notwithstanding the measure, will provide ample incentive to sue. Moreover, the court of appeals was incorrect in believing that damages under Section 20A are unique in being fixed soon after the violation (908 F.2d at 1392); that is ordinarily the case in an action under Rule 10b-5 where the general measure of damages is "out-of-pocket" loss. See *Randall* v. *Loftsgaarden*, 478 U.S. 647, 661-662 (1986) (noting that damages are ordinarily "the difference between the fair value of all that the [plaintiff] received and the fair value of what he would have received had there been no fraudulent conduct"; leaving open the question whether rescissionary recovery may be appropriate in some cases). An out-of-pocket measure of damages does not allow the plaintiff, by "delay[ing] in bringing suit[,] to speculate on the firm's future prosperity," 908 F.2d at 1392. Where rescission is permitted, that measure fulfills a necessary role in deterring intentional fraud. Cf. *Randall*, 478 U.S. at 659; *Pinter* v. *Dahl*, 486 U.S. at 637 n.13 (discussing Section 12(2) of the 1933 Act).

which Anheuser-Busch sued one of its directors alleging that he had disclosed information about Anheuser-Busch's proposed acquisition of another firm to persons who purchased stock in the target company and thereby drove up the acquisition price. H.R. Rep. No. 910, *supra*, at 28. Although Congress did not cover that form of injury in Section 20A, the theory of *Anheuser-Busch* was recognized as a valid basis for recovery under Section 10(b). *Ibid.* As a result, when a defendant misappropriates information from an acquiring company, contemporaneous traders have five years to sue under Section 20A. But, if the one-and-three-year periods apply to other Rule 10b-5 actions, the acquiring firm—a direct victim of the fraud—would have a significantly shorter time to sue for the same violation. Anomalies like that serve no useful purpose and underscore the need for a single, consistent statute.

4. *Section 20A better reflects Congress's current appraisal of the relevant policies.* As a result of the passage of time and "the peculiar blend of legislative, administrative, and judicial history which now surrounds [the] Rule," *Blue Chip Stamps*, 421 U.S. at 749, the force of arguments for choosing the half-century old limitations periods in the 1933 and 1934 Acts for Rule 10b-5 has significantly diminished. For over 40 years, courts assumed that state limitations periods, and not the federal one-and-three-year periods, governed claims under Rule 10b-5. Since the one-and-three-year periods "are shorter than the typical periods in whatever state statutes the courts have looked to traditionally,"[40] applying them would represent a substantial retrenchment from the present state of the law.[41] In contrast, the five-year lim-

[40] L. Loss, *Fundamentals of Securities Regulation* 218 (2d ed. Supp. 1990). The Second Circuit's impression to the contrary in *Ceres Partners*, slip op. 7272, overlooked the fact that borrowed state periods are subject to federal equitable tolling.

[41] That factor may have influenced the American Law Institute's proposed *Federal Securities Code* § 1727(b) (1980), which would have provided a statute of limitations of one year from constructive

itations provision in Section 20A would better approximate the traditional state law periods, while providing the requisite uniformity.

The Seventh Circuit supported its preference for a one-and-three-year provision in part because of its belief that that period alone could secure an outer limit of "repose"; Section 20A, the court thought, may be subject to equitable tolling. *Short*, 908 F.2d at 1391-1392. We agree that the fixing of a defined point of repose is an important structural component of Congress's plan for private securities law actions. But the same benefit is available under Section 20A.

First, although the Court has stated that equitable tolling is "read into every federal statute of limitations," *Holmberg* v. *Armbrecht*, 327 U.S. at 397, the Court, to our knowledge, has never had occasion to apply that principle to a right of action *implied* from a statute containing *express* rights systematically governed by non-tollable limitations periods.[42] That is the situation with respect to Section 20A.

Second, the outside period of repose in the 1933 and 1934 Act periods reflects a general congressional policy against tolling of securities claims that applies equally

discovery and five years from the violation for violations of the antifraud provision. The ABA Task Force proposed "a compromise of two years from the date of discovery, with a four-year cutoff." *ABA Report*, *supra*, at 658.

[42] The three-year period is not subject to equitable tolling. See, *e.g.*, *Data Access*, 843 F.2d at 1550; *Norris* v. *Wirtz*, 818 F.2d at 1332; *Zola* v. *Gordon*, 685 F. Supp. 354, 361 (S.D.N.Y. 1988) (citing cases). A unique limitations principle applies to Section 16(b) (two-year statute of limitations governing claims for recovery of profits realized by certain insiders in transactions involving a purchase and sale, or sale and purchase, within less than six months). 15 U.S.C. 78p(b). Those claims are subject to a quite distinct form of tolling flowing from the related requirement in Section 16(a) that an insider must report his securities transactions to the Commission. See *Whittaker* v. *Whittaker Corp.*, 639 F.2d 516, 528 (9th Cir.) (two-year period is tolled until the insider has filed a required report disclosing his transactions), cert. denied, 454 U.S. 1031 (1981).

to Section 20A. This policy stems from the view that, if tolling is available, potential defendants will be subject to contingent liabilities for indefinite periods.[43] Not only might this "deter [individuals] from serving on boards of directors" because of fear of lingering liabilities, 78 Cong. Rec. 8200 (1934) (remarks of Sen. Byrnes), it could make it more difficult for public companies to "assess the impact of possible litigation under rule 10b-5" for financial statement purposes, thereby possibly adversely affecting the accuracy of their disclosure and "depriv[ing] investors of information adequate for informed evaluation of such companies' potential liabilities" for a longer period of time. *ABA Report*, *supra*, at 646-47.

Third, the language of Section 20A(b)(4) suggests that tolling is inappropriate. In contrast to statutes in which the limitations period runs from the time the "cause of action accrued," [44] Section 20A(b)(4) provides a limitations period that runs from the "date of the last transaction that is the subject of the violation." [45] That is a much more exact starting point, especially since

[43] See 78 Cong. Rec. 8198-8203 (1934); see also *ABA Report*, *supra*, at 655 (finding it "inescapable * * * that Congress did not intend equitable tolling to apply in actions under the securities laws"); Bloomenthal, *The Statute of Limitations and Rule 10b-5 Claims: A Study in Judicial Lassitude*, 60 U. Colo. L. Rev. 235, 257-264, 287-289 (1989) (same).

[44] See, *e.g.*, *Bailey* v. *Glover*, 88 U.S. (21 Wall.) 342, 344 (1874) (equitable tolling of bankruptcy claim).

[45] In the rare instance in which Congress has used language indicating a similarly exact starting point, one court has found the limitations period not subject to tolling. See *Hill* v. *Texaco*, 825 F.2d 333, 334-335 (11th Cir. 1987). We recognize that this Court recently rejected a rule that would have made the availability of equitable tolling against the government turn on the particular "phraseology" of a statutory time limit. *Irwin* v. *Veterans Administration*, No. 89-5867 (Dec. 3, 1990), slip op. 5. But this case is distinguishable, because even if Section 20(A)(b)(4)'s language, standing alone, were not sufficient, it certainly points to the rejection of tolling and the surrounding legislative scheme makes that the most plausible reading of the statute.

courts often view a cause of action as accruing at the date of discovery.[46]

Fourth, barring private actions after five years does not insulate the wrongdoer from all exposure; Rule 10b-5 actions brought by the Commission (except for certain penalty claims) are not subject to any limitations period.

In sum, a five-year non-tollable limitations period drawn from Section 20A would provide a more appropriate statute of limitations than the unduly short one-and-three-year periods, and would be in keeping with the important congressional interest in repose. Against that background, we see no adequate textual, historical, or policy justification for this Court to prefer a limitations period enacted by Congress more than half a century ago, with certain quite different and delimited rights of action in mind, over a limitations period that Congress so recently enacted for certain violations of Rule 10b-5 itself.[47]

CONCLUSION

A five-year limitations period drawn from Section 20A of the Securities Exchange Act, not subject to tolling, should be applied to claims under Section 10(b) and Rule 10b-5.

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[46] See, e.g., *United States* v. *Lovknit Mfg. Co.*, 189 F.2d 454, 457 (5th Cir.) ("Actions for fraud do not ordinarily accrue till the fraud is discovered or should with diligence have been discovered."), cert. denied, 342 U.S. 896 (1951).

[47] If the Court agrees with our view, the case should be remanded to the court of appeals for application of Section 20A(b)(4). Although it appears that most of respondents' claims would be time-barred, the ultimate conclusion is not clear. The complaints (but for respondent Catalan's) were filed on November 3, 1986, alleging fraud in connection with limited partnerships formed in 1979, 1980, and 1981. Claims relating to transactions prior to November 3, 1981, would be time-barred. However, to the extent that installment payments were made after that date (see Resp. C.A. Joint Br. 7), certain claims may survive under the "investment decision" doctrine (an issue on which we take no position). Cf. Note, *Defenses to the Statute of Limitations In Federal Securities Cases: The Fraudulent Concealment Doctrine and the Investment Decision Doctrine*, 38 S. C. L. Rev. 789, 815 (1987).

In addition, the retroactive application of shorter statutes of limitations raises questions under *Chevron Oil Co.* v. *Huson*, 404 U.S. 97, 106-107 (1971). Although Section 20A does not by its terms apply retroactively, see 102 Stat. 4684 (set forth at 15 U.S.C. 78o note), the question whether Section 20A(b)(4) should apply retroactively when *borrowed* for Rule 10b-5 actions is a matter for the courts to determine. Cf. *DelCostello*, 462 U.S. at 169-170 n.21. The court of appeals should initially determine whether such application is warranted here. Cf. *Short*, 908 F.2d at 1389-1390 (citing cases).

Respectfully submitted.

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APPENDIX

15 U.S.C. 78t-1 provides:

Liability to contemporaneous traders for insider trading

(a) Private rights of action based on contemporaneous trading

Any person who violates any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

(b) Limitations on liability

(1) Contemporaneous trading actions limited to profit gained or loss avoided

The total amount of damages imposed under subsection (a) of this section shall not exceed the profit gained or loss avoided in the transaction or transactions that are the subject of the violation.

(2) Offsetting disgorgements against liability

The total amount of damages imposed against any person under subsection (a) of this section shall be diminished by the amounts, if any, that such person may be required to disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 78u(d) of this title relating to the same transaction or transactions.

(3) Controlling person liability

No person shall be liable under this section solely by reason of employing another person who is liable under this section, but the liability of a controlling person under

this section shall be subject to section 78t(a) of this title.

(4) Statute of limitations

No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

(c) Joint and several liability for communicating

Any person who violates any provision of this chapter or the rules or regulations thereunder by communicating material, nonpublic information shall be jointly and severally liable under subsection (a) of this section with, and to the same extent as, any person or persons liable under subsection (a) of this section to whom the communication was directed.

(d) Authority not to restrict other express or implied rights of action.

Nothing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this chapter or the availability of any cause of action implied from a provision of this chapter.

(e) Provisions not to affect public prosecutions

This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this chapter, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties.

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